

EASTERN UNIVERSITY, SRI LANKA
FACULTY OF COMMERCE AND MANAGEMENT
FINAL YEAR FIRST SEMESTER EXAMINATION IN
BACHELOR OF COMMERCE/
SPECIALISATION IN BUSINESS ECONOMICS- 2016/2017
[JANUARY, 2019]
(PROPER)
ECN 4033 – PUBLIC SECTOR ECONOMICS

Answer all questions

Time: Three hours

Number of Pages: 03

Q1. Read the Case Study carefully given below and answer the questions based on it.

Trends in Fiscal Policy

State of Motherland faced adverse consequences of the slowdown in both domestic and foreign demand and the need to provide fiscal incentives to mitigate the impact of local economic crisis. As a result, fiscal management was extremely challenging in the mid of 2018. During the first half of 2018, fiscal operations came under severe pressure mainly due to the lower growth in government revenue, as a result of the slowness in domestic economic activity and decreasing imports. The industries were affected by the economic slowdown, and the burden on consumers increased. Meanwhile, the intensified security situation and the infra-structure projects in the country increased public investment to GDP ratio to 8.6% and interest payments, gave rise to sharp increase in government's recurrent expenditure. During the second half of the year, the impact of unfavourable conditions in the international financial markets negatively affected the domestic economy and significantly, aggravated the pressure on fiscal management. The Government of Motherland could not raise funds from external sources to finance the fiscal deficit. It, thus reduced the domestic borrowing requirement. During the last eight months of 2017, the increased borrowing requirement resulting from the slow performance in revenue and the increased expenditure, coupled with the difficulty in raising planned foreign borrowings due to the uncertain conditions in the international capital markets, increased public debt burden and led the government to depend heavily on

domestic borrowings in financing the budget deficit. In particular, government borrowing from the banking sector increased significantly during the period.

Questions:

- a) What were the "**reasons**" for continuous experience of the deficit in Motherland's fiscal performance during the period? Your reasons should be supported with relevant examples. (08 Marks)
- b) "The mere reduction of public expenditure and the resulting reduction of the budget deficit **is not a characteristic**" of prudent public sector economics". Critically evaluate. (08 Marks)
- c) As a public sector economist, what would you advise for an efficient and effective fiscal policy system? Describe how "**your advice**" could be used by government to regulate the Motherland's economy. (12 Marks)

(Total 28 Marks)

Q2.

- a) Will "**environmental pollution**" lead to "**market failure**"? Give reasons for your answer. (06 Marks)
- b) Does the market make "**environmental damage**"? How? Illustrate. (06 Marks)
- c) How do "**public goods**" prevent "**efficient market condition**"? Analyse. (06 Marks)

(Total 18 Marks)

Q3.

- a) What is meant by "**cost-benefit analysis (CBA)**"? (04 Marks)
- b) "**Many projects are not acceptable**". Do you agree with this statement? If yes, why? If not, how? (06 Marks)
- c) Assume that you are planning to start a project. Show how you would calculate "**costs to compare benefits**" for your project, using a cost-benefit evaluation technique of your choice. (08 Marks)

(Total 18 Marks)

Q4.

- a) Identify the **“three barriers”** that **“prevent other firms”** from entering the market.
(03 Marks)
- b) Is it ‘always’ possible in monopoly that **“public interest”** is best served by having **“only one seller”** in a market? Clarify your answer.
(05 Marks)
- c) Think of a **“monopolist market for computer”**, what benefits would you enjoy when you buy a computer **“already loaded with operating systems”**? Present your answer with suitable examples.
(10 Marks)

(Total 18 Marks)

Q5.

- a) What is meant by **“Pareto efficiency”**?
(05 Marks)
- b) “In welfare economics deadweight loss is the **“loss to society”**”. Do you agree with this statement? Illustrate your answer graphically.
(08 Marks)
- c) How is **“tragedy of the commons”** the obstacle to efficient market? Explain.
(05 Marks)

(Total 18 Marks)